



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Amended:	04/12/05	Bill No:	AB 911
Tax:	Sales and Use Property	Author:	Chu
Related Bills:	AB 1618 (Klehs)		

BILL SUMMARY

This bill would do all the following:

- Require Certified Public Accountants (CPAs), Public Accountants (PAs), and tax preparers to complete a specified number of hours of the required continuing education in the Sales and Use Tax Law, as specified.
- Require business property statements that are filed with county assessors for property tax purposes to include information regarding sales or use tax paid on acquisitions of the property identified on the statements, and allow that information to be shared with the Board of Equalization (Board) and the Franchise Tax Board (FTB), as specified.
- Require county assessors to annually provide an electronic copy of the roll to the Board at no cost.
- Require the property tax statements sent by county assessors to assessees to be accompanied by the form used for filing a use tax return, and require an assessee to file the return and remit any use tax due to the Board.
- Authorize the Board to provide county assessors any information the Board has in its records that will facilitate the assessors' tax administration functions.
- Impose a penalty equal to the amount of deductions and credits claimed by taxpayers on income and corporate tax returns on property for which sales or use tax has not been paid and require the FTB, in conjunction with the Board to prescribe regulations to implement this provision.
- Require the FTB to authorize the Board to administer an audit program to determine whether taxpayers claiming income and corporate tax credits on tangible personal property have paid all applicable sales or use tax on that property.
- Require the FTB to provide all necessary information relating to the taxpayers that are being so audited by the Board.

Summary of Amendments

- The April 12, 2005 amendments 1) add the provisions requiring CPAs, PAs and California tax preparers to include Sales and Use Tax Law within the continuing education requirements, 2) add the provisions requiring county assessors to provide the roll to the Board and to include a use tax return with business property statements, 3) add the provisions authorizing the Board to provide county assessors information that would facilitate the assessors' administration of the property tax,

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and 4) add the penalty and audit provisions with respect to income tax deductions and credits.

ANALYSIS

Current Law

Under specified provisions of the Business and Professions Code, the California Board of Accountancy (CBA) is charged with regulating the accounting profession for the public interest by establishing and maintaining entry standards of qualification and conduct within the accounting profession, primarily through its authority to license. Under these provisions, the CBA, among other things, certifies, licenses, and renews licenses of individual CPAs and PAs, sets continuing education requirements, and monitors compliance with those requirements. Such licensees are required to comply with continuing education requirements adopted by the CBA as a prerequisite to the renewal of their licenses.

The California Tax Education Council (CTEC) is the organization that registers "tax preparers," the second largest segment of tax preparation professionals serving California. Anyone who, for a fee, assists with or prepares a state or federal income tax return, excluding CPAs, attorneys and enrolled agents or their employees, must be registered with CTEC.

The CTEC is charged with providing a list of approved curriculum providers, approving providers of tax education, verifying and registering tax preparers who must obtain a bond.

Under the law, neither the CBA or the CTEC require that the continuing education requirements of CPAs, PAs, or tax preparers include training in the area of the Sales and Use Tax Law.

Under the existing Use Tax Law, Chapter 3 (commencing with Section 6201) of Part 1 of Division 2 of the Revenue and Taxation Code, a use tax is imposed on the storage, use, or other consumption in this state of tangible personal property purchased from any retailer. The use tax is imposed on the purchaser, and unless that purchaser pays the use tax to a retailer registered to collect the California use tax, the purchaser is liable for the tax, unless the use of that property is specifically exempted or excluded from tax. The use tax is the same rate as the sales tax and is required to be remitted to the Board on or before the last day of the month following the quarterly period in which the purchase was made, or to the FTB via the income tax return. A use tax liability is primarily a result of a California consumer or business making a purchase of an item for their own use from an out-of-state retailer that is not registered with the Board to collect the use tax.

Under existing property tax laws, an ad valorem tax is imposed on all assessable personal property used in a trade or business, and its cost must be reported annually to the assessor on the business property statement as provided for in Section 441. The business property statement shows all taxable property, both real and personal, owned, claimed, possessed, controlled, or managed by the person filing the property statement. When the aggregate cost of the taxable personal property is \$100,000 or more, the

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person is required to file a business property statement, signed under penalty of perjury, each year with the assessor.

The content of the business property statement is prescribed by the Board pursuant to Section 452 and is to be used by all assessors. Section 452 specifies that the property statement shall not include any question that is not germane to the assessment function and Section 451 specifies the information furnished in the statement must be held secret by the assessor.

Assessors are required to audit the books and records of a taxpayer engaged in a profession, trade or business at least once every four years if their assessable trade fixtures and business tangible personal property has a full value of \$400,000 or more as provided for in Section 469. Taxpayers are required to make their records available to assessors for examination, including details related to property acquisition transactions, as provided in Section 441.

Proposed Law

This bill would amend the Business and Professions Code to do the following:

- Amend Section 5027 to require a licensee who renews his or her CPA or PA license after January 1, 2006 to complete a minimum of four hours of the required continuing education training in the Sales and Use Tax Law, as specified.
- Amend Section 22255 to require a tax preparer to demonstrate that he or she has, among other things, completed at least four hours of instruction in the Sales and Use Tax Law by an approved curriculum provider, as specified, and, with regard to continuing education, require a tax preparer to complete two hours in education in the Sales and Use Tax Law annually.

This bill would, in addition, add or amend the Revenue and Taxation Code to do all the following:

- Amend Section 407 to require the assessor, on or before August 15, to provide an electronic copy of the roll to the Board at no charge;
- Amend Section 452 to require county assessors to send the form used for filing a use tax return with the business property statement to the assessee; and require the business property statement filed by businesses with the county assessor to include 1) information regarding the business' sales and use tax obligations, and 2) a request for information concerning the business' acquisitions of tangible personal property for which sales or use tax was not paid;
- Amend Section 451 to authorize and require the county assessor to provide to the Board information contained in the property statement when businesses indicate purchases or acquisitions of tangible personal property were made without payment of sales or use tax;
- Further amend Section 451, and add Section 7056.4 to the Sales and Use Tax Law to authorize the Board to provide the FTB any information obtained from the assessor that would facilitate the FTB with its administration of specified provisions of the Personal Income Tax and Corporations Tax Law, as added by this bill;

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- Amend Section 441 to expressly state that details related to property acquisition transactions to be made available to the assessor shall include whether sales or use tax, as applicable, was paid;
- Add Section 7056.45 to authorize the Board to provide to county assessors any information the Board has in its records that will facilitate the assessors' tax administration functions, as specified; and
- Add Sections 17039.3 and 23036.3 to the Personal Income Tax Law and the Corporations Tax Law, respectively, to 1) impose a penalty equal to the amount of a deduction or credit claimed on tangible personal property, if no sales or use tax was paid on the purchase of that property, 2) require taxpayers claiming deductions or credits with respect to tangible personal property to retain sales or use tax receipts, use tax forms, or other evidence of payment of use tax, 3) require the FTB to authorize the Board to administer an audit program to determine if taxpayers claiming credits or deductions have paid all applicable sales or use tax on the tangible personal property, and 4) require the FTB, upon request by the Board, to release all necessary information relating to the taxpayers that are being audited.

The provisions of this bill would become operative January 1, 2006.

Background

The collection of use tax relies heavily on the voluntary compliance of purchasers of tangible personal property. However, due to the general misconception that purchases from outside this state are "tax free" and that audit resources are insufficient to pursue all purchasers, the voluntary compliance rate has been very low. Untaxed purchases from out of state retailers is the largest area of non-compliance the Board's audit staff encounters.

The Board is the state agency responsible for administering the provisions of the use tax. However, in an effort to increase voluntary compliance by purchasers not registered with the Board, legislation enacted in 2003, SB 1009, (Alpert, Ch. 718) requires the FTB to add a line to the state's income tax forms allowing taxpayers to self-report their use tax liabilities to the FTB.

COMMENTS

- 1. Sponsor and Purpose.** This bill is sponsored by the author in an effort to increase use tax education and compliance.
- 2. Enactment of this bill would "get the word out."** Collecting use tax relies heavily on voluntary compliance. This bill would assist in informing and advising taxpayers most likely to be incurring a greater portion of use tax liabilities of their responsibilities under the law. It would also require CPAs, PAs, and tax preparers to include training in the area of Sales and Use Tax Law to meet their minimum continuing education requirements. With over 59,000 CPAs and PAs licensed in California, and over 34,000 registered tax preparers, an educational program in the area of the Sales and Use Tax Law could greatly enhance voluntary compliance.
- 3. The bill would enable tax agencies and the county assessors to work together and share information that would facilitate tax administrative functions.** Proponents note that the bill would enable the tax agencies and county assessors to share the information obtained from the business property statements, the county

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property tax rolls, and the income and corporation tax returns to facilitate administration of California's tax laws. A joint effort by these taxing authorities would provide a framework that would enable California achieve further progress in closing the tax gap.

4. **Personal property statements.** Proponents of closing the use tax gap have noted that local county assessors receive annual property tax statements from businesses related to their personal property holdings that could be used as a data mining source. However, in its present form, the business property statement is not a useful discovery tool. Taxpayers report their personal property holdings by year of acquisition in lump sum amounts that are broken down by a few broad category types. In addition, there are issues with the confidentiality of these property statements as well as their use for other tax purposes, which this bill would expressly address.
5. **Administrative efficiencies in using an existing taxpayer base.** Proponents note that the annual contact that assessors already have with businesses that own tangible personal property at the local level could be a cost effective means to educate and obtain voluntary use tax remittance from businesses as well as provide use tax leads for the Board to pursue.
6. **The enhanced revenues gained by this measure would offset costs.** This bill would require county assessors to use their resources to ensure the use tax return form accompanies the business property statement when provided to assessees, and in processing the use tax questions that would be added to the local property tax statements, and transmitting relevant data to the Board. Proponents note that these additional costs would be offset by the additional revenues local governments would receive. For instance, local governments would receive a share of previously uncollected use tax as well as an increase in property tax revenues, due to the addition of use tax to business personal property assessments.
7. **When would the proposed penalty apply?** The language of the bill appears to impose a penalty equal to any deduction or credit amount that is claimed on income tax returns for any tangible personal property purchased without a timely payment of sales or use tax, or a remittance of sales or use tax with any interest and penalties. It is unclear when the penalty would actually apply. The bill appears to transfer the audit function of the applicability of this penalty onto the BOE. In cases where the BOE makes an assessment of the use tax, together with any interest and penalty, and the taxpayer subsequently pays the liability, would the penalty no longer apply? What if FTB assesses the penalty, and the taxpayer in turn remits the use tax, interest and penalty, would the penalty be canceled? This should be clarified.
8. **Technical amendments.**
 - On page 5, line 14, "22" should be substituted for "20."
 - On page 6, line 38, "on" should be substituted for "for."
9. **Related legislation.** Assembly Bill 1618 (Klehs) would require business property statements that are filed with county assessors for property tax purposes to include information regarding sales or use tax paid on acquisitions of the property identified on the statements and allow that information to be shared with the Board, in a similar manner as this measure.

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COST ESTIMATE

The Board would incur costs attributable to enhancing the audit program to pursue leads from the business property statements, the income and corporations tax returns, and the county property tax roll information, revising the business property statements and associated instructions, educating taxpayers, and responding to taxpayer inquiries. A detailed estimate of these costs is pending.

REVENUE ESTIMATE

A preliminary estimate indicates that enactment of this measure could increase revenues by \$50 million annually. This includes about \$9 million in audit recovery for performing discovery audits on unregistered businesses. The other \$41 million represents an estimate of increased voluntary compliance as a direct result of the provisions of this measure. The incentives to report the use tax timely, e.g. the income tax penalty for failure to remit the tax, and the audit presence from the discovery audit program, is likely to increase voluntary compliance. The \$41 million assumes an approximate ratio of \$5 in voluntary compliance for every \$1 in audit recovery.

Note, voluntary compliance would likely phase itself in over time - we would probably not see significant compliance until after the first year or two. The voluntary compliance estimate is predicated on the assumption that the income tax penalty would remain even after the use tax is paid for those years that a deduction was claimed prior to the use tax being paid. Staff is continuing to review the potential impact enactment this measure would have, and a more detailed revenue estimate will be prepared once this review is complete.

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